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Economic Conditions Governmental Finance United States Securities

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General Business Conditions

THE request of General Eisenhower for more small arms ammunition, announced by the War Production Board November 24, is not only a vivid revelation of the stupendous scope and intensity of the fighting on the German front, but is significant in the domestic situation. Small arms ammunition production was cut back sharply more than a year ago and some plants were closed down, since supplies seemed ample for any conceivable need. Now insatiable demands have made it necessary to raise the schedules again, just as it was necessary earlier to step up the heavy artillery and shell program. The revision adds one more item to the list of munitions which are critically needed, among which heavy artillery and shells, heavy trucks and tires have been prominent. It is fresh evidence of the enormous and changing nature of war requirements, and a fresh illustration of the reason why expectations of any considerable changeover to civilian goods have not so far been realized.

On the European front the war is at its crisis. The rewards of getting more ammunition and more heavy guns to the battleline, in shortening the war and in saving lives and bloodshed, may be inestimable. A defeat of the German armies that are now committed to battle west of the Rhine could cause them such enormous losses — just as the defeat of the Germans in Normandy destroyed whole armies as fighting forces — that they would have little power left for effective resistance.

For a time the lack of port and railway facilities in Europe, which limited the number of ships that could be unloaded and the freight that could be transported, imposed a bottleneck on the supply of our armies. With Mr. Churchill's report that convoys now move into Antwerp, and with improvement of port and rail conditions in France, this bottleneck is being broken and we can ship all we produce. Manifestly it is a time to put forth the greatest effort of which the Army and the country are capable, and none in this country can help more than the people who are engaged in production of these critical items.

Soft-Pedaling Early Reconversion

Although the suddenly-expanded ammunition program will require comparatively little labor and materials, when measured in relation to the whole war effort, it creates problems in particular areas, chiefly the problem of manning the plants. Moreover, the demonstration that the needs of the armies are subject to revision, and that none can foretell how long the conflict will last or how intense the fighting may be, influences Washington policy. The recent tendency is to soft-pedal moves which might be construed as indicating early reconversion. Particularly, the government agencies wish to guard against anything that might cause workers to leave war jobs or make it more difficult for the plants producing the critical items to obtain the workers they need.

Announcement has been made that no further "spot authorizations" of civilian production will be granted for ninety days, in 103 designated areas, and the possibility of ending this program entirely has been mentioned by Mr. Byrnes. The argument for doing so is chiefly that it would have a psychological effect favorable to war production. This argument is not capable of proof or disproof. On the other hand, decisions under the program are made regionally; it is surrounded with safeguards to prevent withholding labor from war work; and its purpose, which is to provide essential civilian goods and give employment to workers who cannot reasonably be expected to move to war centers, does not conflict with the war effort as long as the safeguards are observed. The economic organization needs the goods to be produced, and in due course, as the wear and tear on transportation equipment and similar essentials becomes greater, the program will need to be broadened. These are grounds for arguing that the needed increase in production of critical items should be sought by

specific steps in each case to break the bottlenecks, rather than by new overall measures.

In the industries a good many shifts are taking place from one war item to another, but without much effect on the aggregate of activity. The situation is that there is a demand for everything that can be produced, and production is as high as can be turned out, with regard for the difficulties in keeping factories manned, of increasing or even maintaining efficiency, and of having the right parts and materials in the right place at all times. The Federal Reserve Board's index of industrial production for October was the same as for last July, representing a levelling off in recent months of the declining trend of the first half-year. The manpower situation is not easing and the general experience of manufacturers who have had contract cancellations, and whose labor force has been reduced or dispersed, is that it is hard to find the workers they need when new contracts come in.

Near-Term Prospects

Thus the month's news strengthens the view that no material change in industrial activity or in domestic conditions generally is to be expected until the German war ends. There are few indications that substantial progress will be made either in reconversion or in elaborating reconversion policies, at least publicly. This is not to say, however, that preparations will not go ahead. In many companies the war production program is running smoothly, and higher executives and engineering staffs have more time to give to planning their peacetime products and peacetime operations. These preparations are sure to continue and to bear fruit in smoother reconversion. At the same time W.P.B. has an opportunity to make progress in overall plans.

Whether the cutback in war production after V-E Day will be as great as has been expected is a question on which there is much speculation. Probably all that can be said is that it is impossible to make any certain calculations. It will seem to many observers, however, that the official attitude is based not so much on positive expectations that the German war will run on into next summer as on determination to be entirely safe in covering all possible war requirements, and to be prepared for anything. Business plans should take account of the predominant opinion that the European war may drag on, but also not overlook the possibility that the last great battle which will end it is already well under way.

Pre-Termination Contract Settlement

Among preparations for meeting V-E Day problems and shifting smoothly to peacetime production, the most promising of recent moves is the authorization of "pre-termination planning" for settlement of cancelled war contracts. The country has long realized how tremendous the contract cancellation problem would become, and how urgently prompt settlements would be required, in order to free working capital and plant space, tied up in war goods, for reconversion and reemployment. To prepare to make prompt settlements, it was necessary for the Government to develop policies, obtain legislation, lay down procedures and organize personnel, and for contractors to cooperate. In all these respects progress has been gratifying. At the end of October the Director of Contract Settlement, Mr. Robert H. Hinckley, was able to report to Congress that 28,000 terminated contracts, involving items valued at 9 billions, had been settled by payment of $340 millions, and that the average time required for settlement has been reduced steadily. This is a showing for which credit can be shared widely in both Government and industry.

The real test of the machinery for contract settlement, however, will not arise until the end of the German war, when cancellations will come in a flood. To speed up settlements at that time, by anticipating and preparing for them as far as possible now, pre-termination planning has been devised. Its purpose is to reach agreements in advance and make decisions in advance wherever that is possible, and so avoid delay later.

Settlement of a cancelled contract requires agreement by the contractor and the procurement agency on such matters as the pricing and disposition of the inventory of raw materials and semi-finished goods, the allowance for overhead and indirect and special costs such as "starting load" and settlement expenses, and the rate of profit on unfinished work. It requires decisions on whether tools and machines are to be retained, scrapped or moved, and how items to be turned over to the Government are to be stored or packed and shipped. Under pre-termination planning as many of these decisions as possible are made in advance. For example, agreement might be reached on what the contractor is to pay, per unit, for items which he wishes to retain; and such an agreement would eliminate price negotiation after termination and reduce that part of the settlement to the operation of counting the items and multiplying by the agreed price.

Depending on circumstances, it may be possible to make a formal binding agreement, or only a tentative agreement subject to confirmation at time of termination. Few or many items may be covered. In every case, however, time is saved.

The benefits of such agreements are plain. They will spread the load and reduce the task of settlement at a time when the procurement

agencies may be overwhelmed by the demands upon them. They will enable the contractor to get a final settlement earlier, to get his money earlier, and to get his plant cleared earlier of inventory and machines that obstruct resumption of civilian operations. The third point is of particular importance. In view of the arrangements for partial payments and for interim financing, contractors now feel less fear that their working capital will long be frozen, but the problem of plant clearance is still a haunting one.

Successful operation of pre-termination planning will require cooperation of government agencies and contractors. Contractors are urged to take the initiative, and it is in their interest to do so, and to assign personnel to carry the job through. Widespread application of the plan, by facilitating reconversion, may materially shorten the time during which factories will be out of production and workers out of employment.

"Full Employment—or Else"

In the current discussion of postwar prospects and policies, the most persistently recurring theme is the statement that some fixed number of workers must be employed if the country is to prosper, and that unless "business" provides the stated volume of employment the Government will have to do so,—which means the substitution of a government planned, controlled and subsidized economy in place of the system of private enterprise. Testifying before a Senate Committee last Spring, Mr. Philip Murray, president of the Congress of Industrial Organizations, said that industry, while entitled to reasonable profits for serving the needs of the people, "has an obligation to provide them with full employment." He said:

> We propose that the responsibility shall be placed where it belongs. If industry fails, the American people will give expression to their protest. Let industrialists either deliver the goods with America's gigantic war-born productive capacity or be prepared to give others a chance to use it.

Some business men show by their public statements that they also view "jobs for all" as a challenge which they must meet "or else—." The following is from the New York Herald-Tribune, Nov. 10, 1944:

> Business has a period of between three and five years in which it must demonstrate that it can provide high-level employment, failing which "there is not a man in this room who believes our present form of government will continue," A. D. Whiteside, president of Dun & Bradstreet, Inc., told the twenty-fifth annual meeting of the American Trade Association Executives yesterday in the Pennsylvania. He placed the total of jobs required after the war at 57,000,000, "or 12,000,000 more than we had in 1939."

The view reflected in these quotations is shared by many others. The "challenge" is heard so often that it impresses by force of repetition,—not many people stopping to ask whether it is a fair and valid challenge, and whether business can in fact assume all the responsibility thus placed upon it. The verbal picture of anywhere from 55 to 60 million persons gainfully employed and enjoying a national income of $140 billions or more is so inspiring that people are swept along. Every person in the country wants the goal to be realized, if there are in fact that many who will want gainful work; and there are sound reasons for setting goals, which stimulate effort and evoke courage in business planning. No one dissents from the view that the economic system is not operating at full efficiency and capacity unless there are jobs or opportunities for people who want them and are qualified for them.

Aspirations and feelings, however, should not prevent consideration of the question from all sides. It is too much to expect that "full" or "high" employment can be reached merely by reiterating the need; and no sound purpose is served by describing it as a challenge to any body or group, unless that body or group has power to achieve the goal.

Distribution of Employment

Mr. Murray in the testimony from which we quote referred frequently to employment as a responsibility of "industry." In 1940, when the Census showed aggregate employment of 45,166,000 persons, only 10,573,000, or 23 per cent, were engaged in manufacturing. Adding construction and mining raises the figure to 13,542,000, or 30 per cent, and if retail and wholesale trade, transportation and other public utilities, finance, insurance and real estate are further added, the total rises to 25,662,000, or 57 per cent. The remainder, nearly 20,000,000, were engaged in services of many kinds, in agriculture, forestry and fishing, and in government activities. Thus "industry," in the usual sense of the term, accounted for less than a third of the total gainful employment, and all "business" for only something more than half. This should be borne in mind by those who ascribe responsibility to business.

In 1940, 2,327,000 persons were employed in domestic service, and this kind of employment affords a simple illustration of some of the problems. Who will be "responsible" for giving employment in domestic service after the war? What factors can possibly control the amount of this employment other than the willingness of people to engage in it at rates which other people, who also have a free choice in the matter, are able and willing to pay, and under working conditions which are acceptable to the employer as well as the employe? This does not imply that the conditions of domestic service, as of other work,

should not be improved progressively; but the problem here considered is the problem of *employment*, and the point is that the terms of the employment cannot possibly be ignored. This is a truth which applies in much broader areas.

What Is "Business"?

Many people use the term "business" as if they were referring to an organization like the Army or the Navy, with a hierarchy of authority rising to the top and in which financial and all other considerations are subordinated to the accomplishment of one purpose. A moment's consideration, however, should show that this picture is erroneous. There is no overhead authority in business. The Census of 1940 showed 9,758,000 "employers and own-account workers" (4,600,000 exclusive of farmers), and each is as free and equal as every other. Hence the first observation is that business as a body cannot accept the challenge to provide full employment because there is no such thing as business as a body. The decisions which govern business are not the decisions of a single commander, but of millions of individuals, animated by an infinite number and variety of influences.

These individuals can have work themselves, or give employment, to the extent that they can provide goods or services which people want, at prices which people will pay. At every moment of their lives they are at the mercy of their customers. They cannot guarantee jobs irrespective of wage rates and hours and conditions of work, any more than an individual can guarantee to employ a domestic irrespective of these things. They cannot guarantee jobs irrespective of the costs of what they buy and the prices they must ask for their product; irrespective of consumer preferences; or irrespective of government policies which may affect their costs and profits and stimulate or depress the spirit of expansion and enterprise. They cannot afford to put people to work simply to provide a market for the products of other producers; they can only produce what they can sell, and in the long run sell at a profit. Otherwise there will soon be no business.

It follows that employers of labor cannot possibly bear the whole responsibility of providing full employment. The effort to put responsibility upon them, even if they are willing to accept it, will be unavailing unless equivalent responsibility is put upon labor and the government also, all in a harmonious whole. Mr. Murray, who is demanding that industry provide all the jobs that people want, is likewise active in determining what wage rates and other conditions shall prevail on the jobs provided. Thus he also bears a responsibility, namely, to see that the terms are practicable.

The fundamental condition of full employment and capacity operation of the economic system is a state of balance, in which various prices, wages and other costs, profits, incomes and other elements are in such equitable relationship that all occupations and population groups can exchange their products on terms that will clear the markets. Each group in effect employs the others. Relationships change, and adjustments are required to maintain the balance. Such adjustments require cooperation, which is not always readily given. But they are the responsibility of all groups, not of employers alone.

The Function of an Economic System

Many people will accept the truth of the foregoing, but argue that it does not go far enough. They will rephrase the challenge and say that if the private enterprise system cannot maintain balanced relations, and therefore high employment, some other system dedicated to the maintenance of employment under all conditions will have to supplant it. This is equivalent to proposing to change the function and purpose of economic activity. The primary function of an economic system—under which the welfare of the individual has been bettered throughout history—is not merely to provide jobs, irrespective of the cost and usefulness of the work performed, but to produce an ever more abundant supply of the goods and services which people want, at ever increasing efficiency and declining relative cost. Only a system which accomplishes this will raise living standards and promote the welfare of its members.

If some other system is to be set up which makes employment its primary purpose, the usefulness of the work done will be the subordinate consideration, and it must be expected that work will be wasted, or carried on at a loss out of the public purse. This is the "make work" system, which had no standing in this country before the great depression. It is equivalent, in its economic consequences, to the system that is operative in every country during war. There is no valid evidence that it could operate under peacetime conditions except with the same enormous waste, gigantic cost and inflationary danger associated with war,—to say nothing of the repression of individual liberty, including the liberty of labor.

The Size of the Goal

The danger in drawing the picture of postwar "jobs for all" in terms of a stated figure such as 55 to 60 million people, and in the "or else—" argument, is two fold. One is that the economic system will be judged by the statistics of employment rather than by the standard of living it provides, by its ability to care for people who are not qualified for gainful work and those who are seeking education

or have earned retirement, and by other measures of welfare. The second danger is that the goal itself will be so high as to foredoom the effort to failure.

Figures of the number of jobs said to be necessary are derived from estimates of the total labor force—i.e., the number of people who will normally want gainful employment—in some post-reconversion year. From this total is deducted the number expected to be in the armed forces and the number normally expected to be unemployed at any given time, seasonally, temporarily, or while changing jobs. Estimates of the labor force in 1947, for example, range generally from 58 to 60 million. If 2 to 2½ million should be in the armed forces and the "frictional" unemployment should be 2½ to 3 million, the goal of civilian employment would be 53 to 55 million. The middle of that range, 54 million, is the figure selected by the Brookings Institution, an independent research organization of the highest standing.

This is substantially less than the 57 million referred to in the quotation earlier in this article. The 60 million goal, which is the highest figure ever mentioned, could be supported only by assuming that the total labor force would be 64 or 65 million, which is far above any informed estimate. It is as high as the peak labor force (including the armed services) during the war, when boys have come out of school, older people out of retirement, and women out of the homes to support the war effort.

Factors in the Estimates

All estimates of the postwar labor force, even those based upon the most careful studies of the age groups of the population, must rest upon assumptions. Will the ages at which people enter the working force and retire from it be the same as in the past? Will the same proportion want and need gainful employment? Will they all be employable? How many of the 7 million women who have entered the labor force during the war will want to stay in it? How many returned veterans will take advantage of the educational opportunity provided by the "G. I. Bill of Rights," and return to school?

In answering these questions it is to be considered that an economic system which progressively increases the standard of living will not only produce more goods but yield other benefits. Throughout industrial history these benefits have been realized in the form of a shorter work life, through longer schooling and earlier retirement, of a shorter work week, and of the accumulation of resources for the support of those who are unqualified for gainful work. In the year 1900 nearly half of the young people between the ages of 14 and 20 were gainfully employed, but in 1940 the percentage in the labor force of those between 14 and 19 was only a little over one-quarter, according to the Census. Similarly, of people 55 and over, nearly half were employed in 1900, but only one-third were counted in the labor force in 1940. How much weight should be given to these trends in the future,—how much to the desire and ability of people to take the benefits of industrial progress in more leisure rather than more goods, and of women to remain in the home rather than seek employment? What will be the effect of the huge savings people have accumulated during the war on their choice between work or leisure?

An economic system which gives many people this choice is not to be judged solely by the number of jobs recorded; and with these considerations in mind it may well be asked whether the employment of even 54 million people in the postwar period is desirable from every point of view. The burden of proof is on those who produce these figures to show that the country would not be sound and prosperous with a smaller number at work.

Irrespective of exactly how many more people will want work after the war than in 1940, it will be clear, from the distribution of employment in 1940 as described earlier, that they cannot find it in the industries alone. Services must be substantially expanded. This also is a natural effect of rising standards of living, in which services steadily become more prominent. In the early history of this country 75 per cent of the people were engaged in agriculture and those in the services were few. But in 1940, according to the Census, the number engaged in education, in medicine and health and other professional work, in providing facilities for travel, recreation and amusement, in maintaining household equipment, and in various other services exceeded those engaged in agriculture, forestry and fisheries combined.

Positive harm may be done by setting employment goals at higher figures than are sound and reasonable. Both business and the public may be misled. The result may be disappointment and loss. If responsibility for reaching the goal has been fixed in the public mind upon business or private enterprise, the disappointment and loss will play into the hands of enemies of private enterprise. As opposed to this approach, if the responsibility for employment is placed correctly—that is to say, on *everyone;* if the importance of the terms of employment, of the necessity for investment and of the psychological factors is recognized; and if the policies of all parties are made accordingly, there will be hope not merely of jobs for all, but of useful and self-supporting jobs.

To many people the suggestion that the system of private enterprise may be cast aside if it fails to meet a goal so arbitrarily set up, and a challenge so thoughtlessly formed and repeated, will seem at best shortsighted and at worst dangerously frivolous. It disregards the history of 150 years of economic progress. It passes lightly over the devotion of the American people to the ideal of liberty. It overlooks the magnificence of the response of the American productive system, which has been created by individual freedom and enterprise, to the emergency of war — in meeting our own needs abundantly, in providing immense supplies for our Allies, and in maintaining a high standard of living at home. The "or else—" argument must be judged against these achievements.

Social Security Changes

The question of raising the social security tax for old-age benefit insurance at the beginning of next year has again revealed widespread differences of opinion on this and other phases of the social security program. Freezing the tax rate for another year has been advocated on the ground that the wartime expansion of payrolls has lifted social security tax receipts much above requirements, while benefit payments have been much smaller than estimated; hence that no increase in the tax is needed at this time. During the past three years, large numbers of people over the retirement age of 65 have continued working and paying taxes into the fund, instead of retiring and drawing pensions. As a result, the excess of receipts or "reserve" has built up to a level at least eight times the probable maximum outlay in any of the next five years, whereas a ratio of only three times was contemplated in the law as amended in 1939.

On the other hand, it has been urged that the tax increase now provided by law should be permitted to go into effect, irrespective of the present size of reserves, in order to build them still higher against the needs of the system when millions of persons now covered retire from work and begin to draw benefits. Administration leaders have formally asked Congress for the increase, and Chairman Altmeyer of the Social Security Board has argued that failure to grant it now will mean federal subsidies later on to meet social security obligations. The question is complicated by other considerations, including the many proposed changes in the law for extending the coverage and rounding out the long-range program.

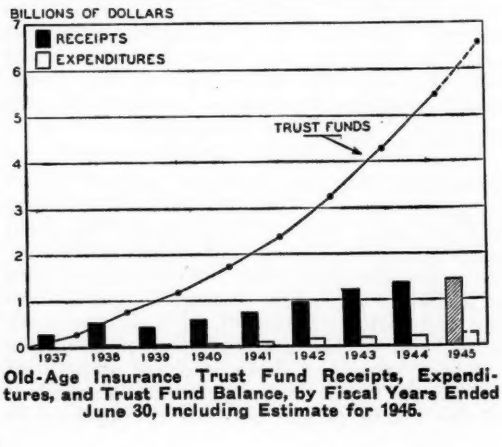
Under the terms of the original Social Security Act of 1935 the tax was scheduled to start on January 1, 1937 at 2 per cent of payrolls up to the first $3,000 annually,— half to be paid by employes and half by employers, and to step up by one per cent (½ for employes and ½ for employers) every three years until a maximum of 6 per cent (3 and 3) was reached on January 1, 1949. In the extensive amendments in 1939 it was provided that benefits should be liberalized and that the statutory increase on January 1, 1940 should not take place, but that on January 1, 1943 the rate should jump to 4 per cent (2 and 2). Before the latter increase became due, Congress postponed the date to January 1, 1944, and again to January 1, 1945, so that as the law now stands the doubling of the rate will automatically take place then unless postponed by act of Congress.

The original law provided that the excess of social security tax receipts over benefit payments should be accumulated in a reserve fund, estimated to reach $47 billion by 1980 and to be invested in government securities, the interest on which, together with current taxes, would balance the benefit payments. The 1939 amendments, however, eliminated the "full reserve" principle and substituted a "contingency reserve" and pay-as-you-go principle, under which each year's benefits would in general be met from that year's receipts.

Growth of the Trust Funds

The table on the following page gives a condensed summary of the transactions in the three trust funds of the social security system from its inception to date, with figures for the current fiscal year ending June 30, 1945 estimated on the basis of actual results for the first five months July-November.

It will be seen that the "Old-Age Benefit Fund", numbered 1 in the table, during the period 1937-45 inclusive will have received a total of over $7 billion from the social security taxes appropriated by Congress, plus $500 million interest on investments. Benefit payments to retired persons, and their survivors, plus administrative expenses, will amount to around



Old-Age Insurance Trust Fund Receipts, Expenditures, and Trust Fund Balance, by Fiscal Years Ended June 30, Including Estimate for 1945.

$900 million during the same period. The $6.6 billion excess of receipts is held in the trust fund or "reserve" and is represented by holdings of special issues of government securities yielding 1⅞ to 2½ per cent, plus uninvested cash.

Benefit payments, although less than estimated, have nevertheless risen rapidly during recent years as the system came into fuller operation. They are expected to expand several-fold more in the future and to reach $4 billion annually by 1980. According to the latest report of the Social Security Board, monthly payments were being made at the end of August to 874,000 retired workers, wives, widows, children, and surviving parents, but the number of actively employed workers, covered by old-age insurance and eligible for future benefits for themselves and families, is around 48,000,000.

Summary of Federal Social Security Trust Funds

(In Millions of Dollars)

Fiscal Years	Tax Rects.	Inter. Rects.	Total Rects.	Total Expend.	Net Rects.	Trust Funds
1. Old-Age Benefit Fund						
1937	$ 265	$ 2	$ 267	$ —	$ 267	$ 267
1938	500	15	515	5	510	777
1939	390	27	417	14	403	1,180
1940	550	42	592	28	564	1,745
1941	688	56	744	91	653	2,398
1942	896	71	967	137	830	3,227
1943	1,130	87	1,217	176	1,041	4,268
1944	1,292	103	1,395	218	1,177	5,446
1945e	1,320	130	1,450	260	1,190	6,636
Total 1937-45e	7,031	535	7,566	930	6,636	6,636
2. Railroad Retirement Fund						
1936	47	—	47	—	47	47
1937	—	—	—	4	— 4	43
1938	99	1	101	76	25	68
1939	119	3	120	106	15	83
1940	120	2	123	113	9	92
1941	113	2	116	121	— 5	87
1942	141	4	144	126	18	105
1943	215	5	220	131	90	195
1944	263	10	273	134	138	333
1945e	325	15	340	140	200	533
Total 1937-45e	1,442	42	1,484	951	533	533
3. Unemployment Trust Funds						
1936	19	—	19	—	19	19
1937	291	3	294	1	293	312
1938	748	15	763	191	572	884
1939	811	27	838	442	397	1,281
1940	921	38	959	514	444	1,725
1941	1,065	49	1,114	555	559	2,284
1942	1,176	67	1,243	377	866	3,150
1943	1,317	82	1,399	177	1,222	4,372
1944	1,470	97	1,567	60	1,507	5,879
1945e	1,530	130	1,660	60	1,600	7,479
Total 1936-45e	9,348	508	9,856	2,377	7,479	7,479
Combined Totals						
1936-45e	17,821	1,085	18,906	4,258	14,648	14,648

"Tax Receipts" represent principally the appropriations to Treasury trust funds of the federal old-age insurance taxes and railroad retirement taxes, and the receipts by the Treasury trust funds of the state unemployment compensation taxes, but include also certain transfers from other funds. "Total Expenditures" represent principally the benefit payments under the old-age insurance and railroad retirement systems, and the withdrawals by states of unemployment trust funds, but include also administrative expenses and certain transfers to other funds. "Trust Funds" are represented principally by holdings of special issues of U. S. Government securities, but include also the uninvested cash balances. e- Figures for 1945 estimated on basis of first five months.

The Railroad Retirement Fund (2), which is similar but is handled separately for railroad employes, includes the private pension plans which many of the large railroad companies had developed for their own workers. This fund should have a balance or "reserve" of over $500 million by the end of the fiscal year.

The Unemployment Trust Funds (3) held in the Treasury come from the state unemployment compensation taxes. The sharp decline in unemployment since 1941 brought a drop of more than 80 per cent in the withdrawals by states for paying unemployment benefits. The fund is currently growing by more than $1.5 billion annually, at which rate it should be around $7.5 billion by the end of the fiscal year. This reserve is greatly expanded because of the war, and represents a substantial fund from which to compensate workers for such short-term unemployment as will be inevitable in the closing down of war industries and the transition to peacetime business.

The totals at the bottom of the table for all three funds combined reveal the tremendous financial scope reached by the social security system in less than ten years of operation. Trust fund receipts for the full period may aggregate almost $19 billion, including $1 billion interest, and expenditures $4 billion, leaving almost $15 billion reserve invested in government securities. The latter is but $1 billion less than the total government debt at its interwar low point in 1930. As the total public debt has risen to over $213 billion at the present time, the portion held by these trust funds has declined to a relatively low percentage, but in dollar amount is very substantial. While these social security transactions are handled outside of the regular budget, and therefore do not reduce the budget or book deficit, the investment of social security tax receipts in government bonds has helped materially in providing cash to finance that deficit in a non-inflationary way.

Other Arguments Pro and Con

Current discussion on the question of whether or not the tax should be raised next month has brought out numerous other arguments both for and against, and has revealed an almost bewildering number of technical questions that must also be considered in extending insurance coverage and rounding out of the social security program to which both major political parties are pledged.

Unless such taxes sooner or later are raised well above the present rate they can never pay for the liberal benefits now offered, and the system must eventually depend upon the Treasury for funds raised by other types of taxation or by public borrowing. It is always easier and more popular to increase the scope

of government payments than to raise the taxes to pay for them.

Another argument for letting the payroll tax increase go into effect now is that the high wartime level of activity and employment should aid both business and workers in absorbing their one per cent increase. This increase has been advocated also as an anti-inflationary move, helping to absorb purchasing power from millions of workers now receiving more money than ever before. An increase has been approved also as a war-financing measure since the social security taxes, although not affecting the budget deficit, help to finance that deficit through their investment in government securities.

On the other hand, the argument already mentioned against raising the tax for the reason that the "reserve" is far above that contemplated in the revised formula is strongly grounded from the legalistic standpoint. Some fear too large a reserve will encourage increases in benefits which in the long run might prove excessive. It has been pointed out too that wartime business and personal tax rates are extremely high and that a doubling of social security taxes, based not upon net income but upon payrolls, would put still more pressure upon all businesses operating on narrow margins of profit or in the red. It might also put pressure upon employes, leading perhaps to demands for higher wage rates to compensate for the tax increase.

Moreover, opposition has been widely expressed to any manipulation of social security tax rates based on considerations having little or no relation to the long-range social security program. Otherwise, the tax earmarked for that particular purpose might be raised or lowered at will, in accordance with Treasury needs for general funds. And, if social security taxes should be raised now, as an anti-inflation measure, would there not be equal logic for lowering them during the next period of deflation?

Many who oppose an increase in the tax rate at this time have tried to make it clear, however, that they are not against the broadening of the social security system, emphasizing the fact that the two proposals are quite separate and distinct. In view of the amendments of 1939 moving the system away from an "annuity" basis toward a "social insurance" (or insurance mixed with relief) basis, and abandoning the "full reserve" principle in favor of a "contingency reserve", the most important point at issue now would seem to be whether or not the obligations of the system require a doubling of the tax rate at this time. There is a lack of harmony between the legal formula for calculating the reserve and the legal provisions for the tax rate, which should be resolved in the light of the other impending changes in the program.

The Need for Further Study

Regardless of what decision is reached as to the tax, there is need for further careful study of the whole system, which has grown so extensive in scope and so involved in operation that any changes made from now on may have serious long-term consequences. The Social Security Board is already a large and complex organization, with a personnel of more than 10,000 in Washington, Baltimore and elsewhere. Many additional amendments must be made in the law and in administrative procedure if the system is to take in millions of people not now covered, including employes with educational, religious, charitable and other "non-profit organizations," with federal, state and local governments, and in domestic service, as well as the large numbers who are self-employed as farmers, in small businesses, and in the professions.

For this reason, the committees studying the social security system in Congress, where even now there are pending more than 185 different bills dealing with one phase or another of the program, will undoubtedly proceed slowly. They will have the benefit of the experience, research and recommendations of the staff of experts connected with the Social Security Board, and also of numerous comprehensive studies of the subject made by other organizations such as the life insurance companies, Tax Foundation, National Industrial Conference Board, U. S. Chamber of Commerce, and others.

Future changes in the system will involve complex and technical matters, on many of which the general public will hardly be qualified to judge. At the same time they will involve broad questions relating to the whole underlying philosophy and aims of the social security program. The danger of over-simplifying the problems will be ever present. The tax rate on old-age insurance, for example, is but one of many phases of the program, and cannot be considered adequately except in its proper relation to private life insurance, group insurance and pension plans, the federal-state unemployment insurance system (including federal advances authorized in the War Mobilization and Reconversion Act of 1944 just passed), postwar planning of public works, allowances in the "G.I. Bill of Rights" to returning members of the armed forces, severance pay to workers released from war industries, state old-age assistance financed 50 per cent by federal grants, federal work-relief or general relief, public health work, and other types of assistance, all of which should be coordinated so far as may be possible.

Likewise, the burden of social security taxes must be considered along with the many other

types of business and personal taxes levied now and in the postwar period by federal, state and local governments. In the final analysis, the success of the program will depend not only upon how ambitious its objectives are, but whether or not the people are able and willing to pay the rapidly rising cost.

It must never be assumed that any system of social insurance and welfare, no matter how elaborate and complete its coverage, and no matter how desirable its aims of ameliorating hardship in individual cases, can ever be an acceptable substitute for a productive system that will create new wealth in abundance. It should be clear that the social security system, despite the large "reserves" now built up, cannot be relied upon as a major support of the country's economy either for postwar readjustment or for long-term growth in general employment, national income and standard of living. The maximum wealth that could possibly be redistributed through any system of social security would be but a minor fraction of the new wealth that is constantly being created and paid out to the people by active business enterprise.

Facts and Fiction Regarding U. S. Balance of International Payments

In the discussion of plans for international monetary stabilization and of the postwar role of the United States in international trade and investment, certain broad statements have been made so often, and frequently with such authority, that they have come to be widely accepted with little or no qualification or proof, and almost taken for granted. It is said, for example, that—

(1) the United States "fell down on the job" as a creditor nation after World War I and, by refusing to lend or buy abroad in adequate amounts, was largely responsible for bringing on the depression;

(2) the United States obliged foreign countries to pay in gold, thus draining off foreign gold reserves and forcing deflation and currency depreciation upon our customers;

(3) our tariff policy was a principal cause of foreign inability to make payments in dollars; and

(4) the United States, as today "the world's greatest creditor nation," ought not only to lower its tariffs with a view to achieving a surplus of imports, but at the same time embark upon a prodigious lending program for the purpose both of meeting the "needs" of the outside world for goods and of maintaining "full employment" at home.

The foregoing are all familiar assertions. The shortcomings of the United States in its experience as a creditor nation have been thoroughly advertised, particularly abroad where a large body of opinion appears to hold this country chiefly to blame for the international economic breakdown of the '30s. This viewpoint was reflected in Lord Keynes's speech on the proposed International Monetary Fund in the British House of Lords last May when, in extolling the virtues of the Fund, he referred to it as "a far-reaching formula of protection against a recurrence of the main cause of deflation during the interwar years, namely, the draining of reserves out of the rest of the world to pay a country which was obstinately borrowing and exporting on a scale immensely greater than it was lending and importing."

The same tendency to treat the United States as the international "bad actor" of the interwar period appears in much American discussion. It crops up—often unconsciously—in our manner of speech, as, for example, where the current issue of the Federal Reserve Bulletin refers to the United States in the '30s as "drawing" money from the rest of the world—as though much of this capital did not come willingly and on its own initiative.

What are the facts? In setting up a postwar international monetary program we need to start from sound premises. Since it is generally recognized that the balance of payments position of the United States is at the heart of the problem, the first task would seem to be to get a clear picture of what that position actually was between the close of World War I, when the United States emerged as a creditor nation, to the outbreak of World War II in 1939. This can be done most readily by dividing the eighteen-year period, 1922-39, into two nine-year periods, 1922-30 and 1931-39. The figures appear in the table on the following page.

Analysis of the Facts

The first thing to be noted in the table is that on goods and service account the United States was not—as so often charged—persistently collecting more abroad than it was willing to expend abroad. While it is true that on merchandise account alone we were selling more than we were buying, we were at the same time making substantial net expenditures abroad for such purposes as immigrant remittances and charity, travel, shipping services, etc. As a result, our total outlays for such items abroad actually *exceeded* our receipts abroad for each nine-year period. On current account for goods and services we were debtor, not creditor.

As the 1943 Annual Report of the Federal Reserve Bank of New York pointed out in an illuminating article on "Postwar International Monetary Cooperation," the residue of truth in foreign beliefs about our international transactions in goods and services is that our

U. S. Balance of International Payments in the Interwar Period

(In Billions of Dollars. Plus signs indicate net receipts by U. S., and minus signs net payments by U. S.)

	9 Year Periods 1922-30	1931-39
Goods and Service Transactions		
Net Goods and Services Sold		
Excess of merchandise exports	$+6.5	$+3.9
Net Goods and Services Bought		
Net immigrant remittances and charity	—3.1	—1.7
Net tourist expenditures	—2.4	—1.6
Net shipping expenditures	— .7	— .7
Other (net) transactions, incl. silver purch.	— .5	— .9
Total	—6.7	—4.9
Net Goods and Service Transactions	— .2	—1.0
Financial Transactions		
Debt Service and Dividends		
Net interest and div. receipts (private)	+5.1	+3.0
Net amortization receipts (private)	+1.9	+1.4
War debt payments to U. S.	+1.7	+ .1
Total	+8.7	+4.5
Other Financial		
New long-term loans and direct invest.	—9.8	— .8
Repatriation of foreign securities	+ .6	+ .5
Net sales of U. S. securities abroad	+1.9	+1.5
Net short-term capital inflow	+ .2	+2.4
Total	—7.1	+3.6
Net Financial Transactions	+1.6	+8.1
Balance of All Above Transactions	+1.4	+7.1
Balancing Items		
Gold Movement (a)	— .7	—9.7
Residual total (b)	— .7	+2.6
Balance	$—1.4	$—7.1

Source: "The United States in the World Economy." U. S. Dept. of Commerce. (Economic Series, No. 23)

a—Gold imports designated with minus signs as representing expenditure of U. S. dollars. b—Difference between calculated net balance of all transactions and gold movement. During the '20s the minus residual reflected underestimation of payments from the U. S., including unreported trade credits and speculative purchases of foreign currencies. During the '30s the plus residual reflected underestimation of payments to the U. S., including unreported inflow of refugee capital.

purchases did not exceed our sales by a sufficient margin to offset the outside world's need for dollars for private interest and dividend payments and war debt transfers. During the '20s these requirements were more than covered by a heavy outflow of capital from this country in the form of long-term loans and direct investments. The net imports of $700 million of gold were amply accounted for by a voluntary inflow of foreign capital for repatriation of foreign securities, investments in our stock market, and building up of short-terms balances here.

During the '30s, when our long-term capital exports were drastically reduced, the dollars for foreign debt service and dividend requirements were indeed supplied in part through gold shipments. Yet, as the table shows, the total of such requirements not covered by our debit balance on current goods and service transactions and on long-term capital account was considerably less than a third of the $9.7 billion of gold imports during the period. The rest of the gold came as a capital movement, due very largely to economic and political uncertainties abroad.

In short, criticism of the United States as a creditor nation would seem warranted not for "obstinate" failure to provide enough dollars, but rather for first providing too many dollars and for wrong purposes, and then suddenly cutting down the flow. The trouble was we went to extremes. At the same time, the responsibility of foreign countries for accentuating the scarcity of dollars through capital transfers to this country should also be emphasized.

In any review of the balance of payments experience between the two wars, the disturbing elements that stand out overwhelmingly have been the sudden movements of capital—both American and foreign—and the instability of our internal economy, with consequent wide fluctuations in our imports and other expenditures abroad. In the face of these sweeping movements the influence of American tariff rates upon our overall balance of payments and upon the supply of dollar exchange seems clearly subordinate.

Of course, the objective is not merely to achieve a balance between incoming and outgoing payments, but to do so at the highest level consistent with a steady and orderly flow of reciprocal goods and services. During the '20s the whole level was dangerously inflated by excessive expansion of credit, while during the '30s the balance was achieved partly at the sacrifice of payments on war debts and an important share of interest and dividends due us on private investments.

Our Creditor-Debtor Position

As for the references to our being "the world's greatest creditor nation" and to our obligations as such, it is doubtful if there is general realization of how much our net creditor position has been whittled down from the high point between wars. The war debts of course have long ceased to be paying assets. As for private investments, the following table, adapted from a Department of Commerce report, shows that the excess of such U. S. investments abroad over foreign investments here dropped from $9.5 billion in 1933 — which probably was around the peak — to $1.8 billion in 1939.

The decline in our net creditor position shown in the table was due principally to (1) a decrease in our portfolio investments brought about by redemptions and repatriation of securities from American markets, fre-

International Investment Position of the United States, Exclusive of War Debts
(In Billions of Dollars)

U. S. Investments Abroad	1919	1930	1933	1939
Long-term investments—				
Direct	$ 3.9	$ 8.0	$ 7.8	$ 7.0
Portfolio	2.6	7.2	6.0	3.8
Total long-term	6.5	15.2	13.8	10.8
Short-term investments	.5	2.0	1.1	.6
Total invest. abroad	7.0	17.2	14.9	11.4
Foreign Investments in U. S.				
Long-term investments —				
Direct	.9	1.4	1.8	2.0
Portfolio	1.6	4.3	3.1	4.3
Total long-term	2.5	5.7	4.9	6.3
Short-term invesments	.8	2.7	.5	3.3
Total foreign invests.	3.3	8.4	5.4	9.6
Net creditor position of U. S.	$ 3.7	$ 8.8	$ 9.5	$ 1.8

Source: "The United States in the World Economy," U. S. Dept. of Commerce. (Economic Series No. 23)

quently purchased at substantial discounts from par, and (2) a building up of foreign investments in this country, chiefly in American stocks, bonds, short-term investments and bank balances. Considering the fact that the $3.8 billion of U. S. foreign portfolio investments remaining in 1939 were counted at par values well above market values, and included securities in default, even the $1.8 billion net creditor position shown for that year appears high. The question may well be raised as to whether in terms of actual values it had not been entirely wiped out.

To what extent the war has affected our creditor-debtor position cannot yet be determined. But with the destruction that has been wrought in many areas, and with the further accumulation of foreign funds in this country, due both to the influx of flight capital and to heavy U. S. purchases of foreign materials, the probability of our being a creditor nation in the sense of having "good" investments abroad in excess of foreign investments here becomes still more dubious. In fact, the indications suggest the reverse, unless war debts and lend-lease be considered collectible assets.

Moreover, whereas our own investments abroad are mostly long-term, a large share of the foreign investments in this country consists of highly liquid securities and demand obligations which could be withdrawn on short notice. According to the latest Treasury figures the total of such short-term investments and bank balances alone amounted to $5.4 billion in July of this year, against $3.3 billion in 1939.

It is true that on a current interest and dividend basis the United States continued to be a substantial creditor in 1939 — by approximately $300 million, according to the Department of Commerce. This was explained as largely because new foreign investments in the United States during the '30s included large amounts of short-term assets, the earning power of which was negligible, while the reduction in United States investments abroad was concentrated in portfolio and short-term holdings, leaving the more profitable direct investment stake substantially intact. But these figures, too, may have been affected substantially by the war.

The Kind of Program Needed

The foregoing is not to suggest that the United States will not and should not be prepared to cooperate in the postwar period in the providing of credit and capital for foreign reconstruction and development, and in the encouragement of multilateral trade through mutual efforts toward breaking down excessive trade barriers. The United States, with its great productive capacity, will be wanting foreign markets and in the development and financing of its foreign trade will continue to be a great capital exporting country. As such, our interests will call for international monetary collaboration, and for recognition in our trade policies of the need for a two-way flow of goods and services if trade is to prosper and the sums loaned abroad are to be repaid.

In setting our sights for the future, however, we need to be realistic and not be misled by slogans. We need first to get the facts straight as to our past and present position, and to apply the lessons to the future. A danger is that we shall again pour out money in loans abroad without adequate consideration of how we are going to get it back; and that when we find we have poured out too much we shall suddenly stop and repeat the experience of the '30s. What is wanted is a flow of investment in such amounts and to such productive uses that a steady stream of debt service and dividends can be maintained. The continuity and character of investments and trade are more important than the absolute amount at any time.

With respect to the balance of trade, it is clear that if we want to stimulate exports we must also stimulate and permit imports. The latter means primarily the maintenance of a high volume of business activity and consuming power in this country, and secondarily, a reconsideration of the tariff. If we can have the first, together with a tariff policy based upon the principle of holding down rate increases, and seeking opportunities for such downward adjustments as may be found possible and desirable from time to time in exchange for similar concessions by other countries, the results should be an enlargement of two-way trade to the mutual benefit of ourselves and the rest of the world.

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